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Public-Private Partnerships: an International Development vis a vis *Indonesia Experience*

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ABSTRACT

For more than two decades, Public Private Partnerships (PPP) had developed worldwide as an instrument to procure public infrastructure where government funds are limited. This practice supports the covergent theory of the public and private sector. Indonesia experience with PPP follows most of what had been done by countries overseas with some deviations. The main reasons for going for PPP for Indonesia government is to fill the gap in finance and capability in procuring the infrastructure. Unofficial reason such as for off-balance sheet and ideological is not relevant. Up to now, the Government only allow investment in hard economic infrastructure. Instead of using pure private finance, Indonesia Government facilitates public funds either from Central Government or Local Governments to finance PPP projects. In most cases, this involvement is because of marginality of the project. This results in the condition where the Government still has dominant role in the existing PPP projects. Compared to the PPP framework in other countries like in the UK, Indonesia PPP lacks of attention on output specification and risk transfer. This may be because of lacking of experiences as well as due to high degree of Government involvement. Rigorous policy is needed in this area to ensure Government to achieve better value for money.

Keywords: Public-Private Partnerships, Public Infrastructure Procurement, International PPP, Indonesia PPP, value for money mechanism

INTRODUCTION

Growing demand for public infrastructure in the context of limited public funds has pushed governments in many countries to see more private sector involvement in infrastructure procurement. Since 1990s, this involvement has moved to an integrated model of a Public Private Pratnerships (PPP) contract which bundles the design, construction, financing and operation activities into a single long-term contract.

Hodge et al (2010, p. 595) noted that the importance of the PPP has increased worldwide. From Table 1, it can be seen that a number of countries, such as Spain, Italy, the United States and Canada increased their use of the PPP procurement route. Meanwhile, the UK, was the country with greatest PPP investment in the mid-2000s (Yescombe, 2007, p. 30). Kappeler and Nemoz (2010, p. 8) reported that the UK was, by 2009, the largest PPP country with the investment portfolio, comprising 52.5% of the total PPP investment in European countries.

Cuttaree and Mandri-Perrott (2011, p. 8) noted that global PPP investment rose from 2005 to 2007. However, in 2008 there was a slight decrease as an effect of the world financial crisis and a greater decrease in 2009 as the crisis went on. In contrast, there is a growing phenomenon since 2009 that middle income countries, such as Brazil, India, Russia Turkey and South Africa, increased their use of PPP which contributed to worldwide PPP investment increases (p. 15). Hawkesworth (2011) stated that, based on an OECD survey, the percentage of public sector infrastructure investment through PPP varies among countries and can reach more than 20%. Table 2 shows that two countries (Mexico and Chile) are using PPP for more than 20% of public sector infrastructure investment. They are followed by South Korea with a percentage of between ten to 15 and another seven countries including the UK with percentages of between five and ten (Hawkesworth, 2011).

The development of the PPP market has been growing in different stages. In Figure 1, Deloitte (2006) classified the worldwide PPP market, based on its sophistication and activities. Countries in stage one are those with the lowest level of market maturity. They focus PPP activities on establishing policy, initiating a central unit to guide implementation, developing deal structures and public sector comparators, building the new marketplace, and

TABLE I: INTERNATIONAL PUBLIC PRIVATE PARTNERSHIP PROGRAMMES

	2003		2004		2005	
	PPPs	Value US $m	No. PPPs	Value US $m	No. PPPs	Value US $m
United Kingdom	59	14,694	86	13,419	62	10,723
Spain	8	3,275	7	2,778	10	7,092
Italy	3	714	2	1,269	8	4,504
United States	2	927	3	2,202	5	3,304
South Korea	3	3,010	9	9,745	4	3,179
Canada	n/a	n/a	3	746	5	3,157
Australia	4	611	9	4,648	9	2,221
France	0	0	0	0	3	1,208
Japan	5	274	15	1,473	11	675
Portugal	n/a	n/a	2	1,575	3	481
Hungary	1	251	2	1,521	n/a	n/a

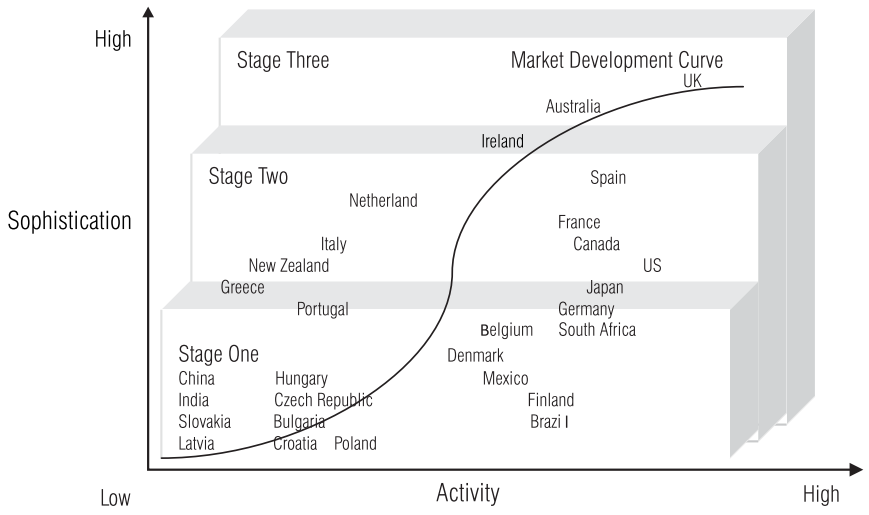
Source: Dealogic in Yescombe (2007)

TABLE 2: PPPS' PERCENTAGE IN PUBLIC SECTOR INFRASTRUCTURE INVESTMENT

RANGE	N	COUNTRY
0% - 5%	9	Austria, Germany, Canada, Denmark, France, Netherlands, Hungary, Norway, Spain
5% - 10%	7	United Kingdom, Czech Republic, Slovak Republic, Greece, Italy, South Africa, Ireland
10% - 15%	2	Korea
15% - 20%	0	
more than 20%	20	Mexico, Chile

Source: Hawkesworth (2011)

FIGURE1: PPP MARKET MATURITY CURVE



Source: Deloitte (2006, p. 6)

applying early lessons from transport to other sectors.

Countries in stage two focus on developing new hybrid delivery models, expanding the PPP marketplace, leveraging new sources of funds from capital markets and using PPP to drive service innovation. Countries with a high level of maturity, such as the UK and Australia, focus on refining new innovative models, developing more flexible approaches to the roles of the public and private sectors, providing more sophisticated risk models and infrastructure, giving greater focus to the total lifecycle of projects, and increasing the learning of the public sector from private partners.

In Indonesia, the PPP is developed after decentralisation reform in 2000s and starts to be used intensively in the last few years. Based on Strategic Asia's (2012) assessment, in terms of market maturity, Indonesia can be categorised under stage two where the Government had undergone establishing policy, building new market and developing non-transport PPP and now focusing on PPP market expansion. This article aims at analysing Indonesian's experience with PPP as compared with International development. The analysis focuses on comparison on how International PPP especially and Indonesia PPP is developed, reasons for the PPP and mechanism in project assessment. This comparison is useful to identify deviations and how they may affect PPP development.

THEORETICAL FOUNDATION OF PPP DEVELOPMENT

The term 'public sector' is associated with governmental activity. This can be seen from the early studies of the public and private sectors which refer to the comparison between public agencies owned collectively by members of political communities and the private firms owned by entrepreneurs or shareholders (Boyne, 2002). In this area, organisation theorists have come up with two different accounts which some describe as different in nature but others describe as convergent (Allison, 1979; Boyne, 2002; Hughes, 2003; Rainey et al, 1976).

From the literature it can be seen that there have been some changes in the nature of the differences between the public and private sectors. Higher degrees of differences in the past have diminished. Rainey et al (1976) argued that the government aspects are so wide, varied and continually evolving that it is difficult to draw a clear line. They further explained that there are two interrelated phenomena that have made the public sector more convergent on the private sector: first the intermingling of governmental and non-governmental activities; and, second, the increasing similarity of function, context and role of the public sector with the private sector. Rainey (2009) considered that there is little difference between public and private organisations. He explained that an organisation's tasks and functions have more influence on organisational characteristics than the status of being public or private. This argument suggests that, if the public sector has similar tasks and functions to the private sector, they can be carried out by the private sector.

One area, where public sector is largely similar with private sector, is infrastructure procurement. Yescombe (2007) said that public infrastructure can be classified either by function or by form. In terms of function, public infrastructure can be categorised into economic infrastructure and social infrastructure. Economic infrastructures are those which are expected to enhance productivity and innovation (Grimsey and Lewis, 2004). Economic infrastructure can be classified based on its form into hard or soft economic infrastructure. Hard economic infrastructure includes roads, highways, bridges, ports, power and telecommunications: soft economic infrastructure covers vocational training, financial facilities for business transaction, research activities, technology transfer and export assistance. Social infrastructures are those which are needed for the structure of society and relate to providing basic services to households (Grimsey and Lewis, 2004). They can be classified further, based on their forms, into hard or soft social infrastructure. Hard social infrastructure encompasses hospitals, schools, water supply, sewerage, housing, prisons and care homes for the elderly: soft social infrastructure include social security, community services and environmental protection programmes.

The Public Private Partnerships (PPP) was introduced in 1992 by the then UK Conservative Government under the term Private Finance Initiative (PFI). Later, the Labour Government introduced the term 'Public Private Partnerships', referring to similar transactions. Treasury (2000), in its document 'Public Private Partnerships – The Government's Approach' defined the PPP as:

> *the public sector contracts to purchase quality services, with defined outputs, on a long-term basis from the private sector, and including maintaining or constructing the necessary*

> *infrastructure. The term also covers financially free-standing projects (e.g. the Second Severn Bridge) where the private sector supplier designs, builds, finances and then operates an asset and covers the costs entirely through direct charges on the private users of the asset, with public sector involvement limited to enabling the project to go ahead through assistance with planning, licensing and other statutory procedure (p. 47).*

This definition suggested that the PPP procurement route is not aimed at buying an asset as what the government does in conventional procurement but at buying the required services for a lengthy period. In addition, PPP is applicable for services which are paid for by either the public authority or the end-users.

The UK then pionereed the development of PPP around the world, but the PPP definition does not necessarily refer to the idea of buying services as strictly in the UK. The Canadian Council for PPP for instance defined PPP as 'a cooperative venture between the public and private sectors, built on the expertise of each partner, that best meets clearly defined public needs through the appropriate allocation of resources, risks and rewards.' Unlike the UK way which separate the role of public and private sector, the Canadian PPP open the opportunity for both the public sector in the activity of design, build, finance and operate based the appropriate allocation of resouces, risk and rewards (Siemiatycki, 2013).

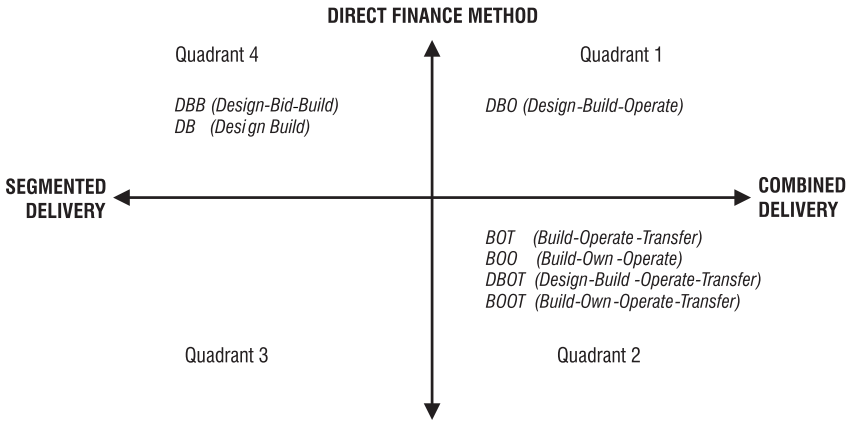
The Ministry of Finance of Singapore (2004) defined PPP as 'long-term partnering relationships between the public and private sector to deliver services. It is a new approach that Government is adopting to increase private sector involvement in the delivery of public services.' According to KPMG (2007), in Singapore, PPP is seen as a way of bringing in specialist private sector expertise to stimulate an exchange of ideas and bring more international players into the domestic market (KPMG 2007). Meanwhile, In India, the Department of Economic Affairs of the Ministry of Finance (2005) defines PPP as 'a project based on contract or concession agreement between a Government or statutory entity on the one side and a private sector company on the other side, for delivering an infrastructure service on payment of user charges.' This definition focuses on Government's concession to the private sector to develop a project and provide services in return for payment of user charges. The public sector's engagement in the Indian PPP is limited to the granting of the concession, owing to financial constraints and lack of modern technology.

In Indonesia, the initial regulation promoting the use of PPP after the 1997 financial crisis was Presidential Decree no 67/2005. This regulation suggested public infrastructure to be procured through partnerships with business entities such as private companies, state owned enterprises (BUMN), Local Government Owned Enterprise (BUMND) and Cooperatives. In that regulation, some characteristics of PPP are incorporated that the purposes of the partnerships are: (1) to finance the project through private sector involvement; (2) to improve service's quantity and quality through healthy competition; (3) to improve the quality of project's management and maintenance; (4) to push the implementation of the principle of the users pay for the service received. PPP definition is stated in Presidential Decree (Perpres) no 13/2010 as 'infrastructure procurement through partnership agreement or concession granting between ministry/Head of Government Body/Head of Local Government with Business Entity.' Again, this definition is considered as a broad terms which does not limit PPP to buying service as pioneered by the UK PPP. The advantage of this broad definition is facilitating government to have variations in project arrangements based on available resources.

PPP DELIVERY METHODS

Grimsey and Lewis (2005, p. 346) stated that PPP procurement is used to fill the gap between conventionally procured Government projects and full privatisation. In addition, Ball and King (2006) differentiate PPP and conventional procurement in three aspects. First, conventional procurement only includes infrastructure procurement in its contract. However, under the PPP, the contract also includes private sector involvement in financing and in post-construction activities, such as infrastructure operation and maintenance. Second, instead of specifying how the infrastructure should be designed and procured, the PPP contract adheres to output specification provided by the client who describes the services that the public sector client needs. This approach is expected to enable PPP bidders to come up with the best design that the private sector can offer to serve these needs at an affordable cost. Third, significant

FIGURE 2: CLASSIFICATION OF PROJECT DELIVERY METHODS



Source: adapted from Pietroforte and Miller (2002)

risks associated with the project should be transferred from the public sector client to the private sector. Among the three aspects, the OECD (2008, p. 18) considered risk transfer to be the fundamental feature which differentiates PPP from conventional procurement.

The difference between conventional and PPP procurement can also be analysed from two dimensions as suggested by Pietroforte and Miller (2002), namely financing and delivery. The financing dimension can be either direct or indirect. Direct finance is procurement which is fully funded by the public sector, while indirect finance is procurement fully funded by the private sector. The project procurement dimension comprises either segmented delivery or combined delivery. Segmented delivery is a method of procurement where each activity is undertaken under a separate contract. In contrast, combined delivery is procurement whereby all activities are undertaken under a single contract with the private sector. The relation of the two dimensions is captured in the four quadrants in Figure 2.

The four quadrants examine the combination of project delivery and methods of financing. Quadrants 1 and 4 show the situation where the private sector has the least role in financing activity. In these quadrants, the private sector does not have any responsibility to provide the needed funds. The difference between Quadrant 1 and Quadrant 4 is on the degree of procurement activities. Projects in Quadrant 4 undertake only one activity in a single contract. Projects in Quadrant 1 are allowed to undertake all the procurement activities in a single contract. In Quadrant 2, the private sector has the greatest role in both financing and infrastructure delivery. Procurement in Quadrant 2 shows that the private sector has responsibility for providing funds and performing all procurement activities. The procurement method in Quadrant 2 the subject of this thesis) represents the characteristics of PPP, while Quadrants 1 and 4 represent the conventional types of procurement. Quadrant 3 is blank because no delivery method exists with the combined charactistics of segmented delivery and indirect finance.

Indonesia first experience with PPP type project is Tangerang Merak Toll project in 1987. Prior to this project, all toll roads were solely managed by PT Jasa Marga as a state owned company. This early model is more similar to joint venture where the government has significant share in project company. It used modified BOT model with a private company where the Government also participated in financing the project (Pradono et al, 2012). Table 3 shows toll road projects managed by the private sector in Indonesia and how they are financed. Among eight toll networks managed by the private sector, six used modified BOT and only two purely used BOT. The BOT model is relatively similar to the origin PPP developed in the UK where the financing of land acquisition, construction and operation and maintenance is fully funded by the private sector. However, through modified BOT, some parts of construction and land acquisition are expected to be financed by the government. Consequently, under this modified model, the main PPP characteristics in terms of risk transfer will not properly applicable.

REASONS FOR USING THE PPP

Based on the experience of other countries such as the United Kingdom, there are a number of reasons suggested for the extensive use of the PPP. These can be categorised into official and unofficial reasons. The official reasons are those stated by the government, while the unofficial reasons are those interpreted by the public, especially academics or public policy observers. The following sub-sections discuss the two categories.

1. OFFICIAL REASONS

The PPP policy was adopted by the UK Conservative Government in 1992 and continued by the Labour Government from 1997 until 2010. In their official statements, Governments of both persuasions have stressed achieving greater investment and VFM for tax payers as the main purposes for using the PPP.

I. GREATER INVESTMENT

Ford and Zussman (1997) said that in the 1980s, governments considered two alternative mechanisms for engaging the private sector: total privatisation of public facilities and PPP. The privatisation enables governments to transfer to the private sector the total responsibility for developing, managing, and providing public services. However, through PPP, governments are able to invite private sector entities to finance and develop infrastructure projects without losing state control over the regulatory aspects of service provision, including the pricing of the services provided by the infrastructure facility (Abdul-Aziz 2007). In its development, PPP became the popular option rather than privatisation which controversial politically. Further, governments were hesitant to subject certain facilities to total privatisation for reasons such as national security.

In Treasury's (2000) 'Public Private Partnerships: The Government Approach' state that the suggested reforms to the PPP policy were expected to result in significant increases in the contribution made by private finance to publicly-sponsored total gross investment, from 10% in 1998-99 to an average of 15% in 1999-2000 to 2001-02 (p. 13). This contribution was predicted to increase following further reforms to the PPP to extend the scope of public sector activities to which this procurement method could be applied.

In its 2013 PPP book, Indonesian Ministry of National Development Planning (MNDP) also used similar argument on the need for PPP. It is said that by 2013, Indonesia's infrastructure investment to total output is at around 3% which is below its pre-financial crisis level of around 7% (MNDP, 2013, p. vi). The book quoted a UN report that infrastructure investment is urgently required because of rapid urbanization in Indonesia. Prior to this, in a report published by OECD, it is said that public spending on infrastructure in 2009 was only 1.9% of GDP.

In May 2011, Indonesian Government launched a development strategy called Master Plan for the Acceleration and Expansion of Indonesia's Economic Development (MP3EI) published by the Coordinating Ministry of Economic Affairs (CMEA) (2011). The then President Yudhoyono said that this national strategy aims to leapfrog Indonesia into the ten biggest economies by 2025. The strategy is expected to increase GDP to US $4.5 trillion as well as by increasing GDP per capita income from a current level of US$ 3000 to US$ 15,000. The master plan suggests Indonesia development is based

TABLE 3: TOLL ROAD NETWORKS MANAGED BY THE PRIVATE SECTOR

NO	TOLL ROADS	LENGTH (KM)	PROJECT COMPANY	START OPERATION	DELIVERY METHODS
1	Tangerang – Merak	73.00	PT. Marga Mandala Sakti	1987-96	Modified BOT
2	Ir. Wiyoto Wiyono MSc	15.55	PT. Citra Marga Nusaphala Persada	1990	Modified BOT
3	Surabaya-Gresik	20.70	PT Margabumi Matraraya	1993-6	Modified BOT
4	Harbour Road	11.55	PT. Citra Marga Nusaphala Persada	1995-6	Modified BOT
5	Ujung Pandang Tahap I	6.05	PT. Bosawa Marga Nusantara	1998	BOT
6	Serpong – Pondok Aren	7.25	PT. Bintaro Serpong Damai	1999	Modified BOT
7	SS Waru Bandara Juanda	12.80	PT Citra Margatama Surabaya	2008	Modified BOT
8	Makassar Seksi IV	11.60	PT. Jalan Tol Seksi IV	2008	BOT

Source: Indonesia Toll Road Authority, Ministry of Public Works (2008) and Pradono et al. (2012)

on six economic regions or called 'Six Corridors'. Each corridor has its own theme and focus of economic development: Sumatra Economic Corridor as a center for production and processing of natural resources and as nation's energy reserves; Java Economic Corridor as a driver for national industry and service provision; Kalimantan Economic Corridor as a center for production and processing of national mining and energy reserves"; Sulawesi Economic Corridor as a center for production and processing of national agricultural, plantation, fishery, oil & gas, and mining; Bali – Nusa Tenggara Economic Corridor as a gateway for tourism and national food support; and finally Papua – Kepulauan Maluku Economic Corridor as a center for development of food, fisheries, energy, and national mining.

The total investment for the six corridors will amount to Rp. 4,012 trillion and 43% of which will be channelled towards infrastructure development (CMEA, 2011). To fund the program, the private funding is projected to contribute to 51% of the funding, or Rp. 100 trillion per year. In 2010, the Coordinating Ministry of Economic Affairs targeted to raise fund IDR 980 trillion under the PPP scheme (CMEA, 2010). This amount is equivalent to more than 68.5% of its IDR 1,430 trillion infrastructure investment required at the national level over the period 2010-14.

Looking at the projected time span, the target seems ambitious and doubtful to reach. Based on the experience with first big PPP projects in power plant, it took 39 months to complete a process from the beginning to financial close. This duration is much longer than projects neighboring country like Singapore (18 months), or Canada (18 months) and the UK (30 months) (Strategic Asia, 2012). Assuming, the same condition still exist, the timetable to achieve the expected target needs to be revised. Otherwise, improvement in PPP framework mechanism needs to be simplified, resources who manage the procurement process needs to be improved and best practices need to be shared and adopted to address problems,

II. VALUE FOR MONEY

Value for money is another reason for governments to use PPP schemes. In an annex to the statement 'Public Private Partnerships: The Government Approach', the UK Treasury addressed the cost overruns and delays in some traditional procurement contracts which might be alleviated under the PPP procurement route. The following Table shows problems that were identified in some projects under conventional procurement.

Mott MacDonald (2002) studied the delays and cost overruns in both traditional and PPP projects in the UK. They examined 39 traditionally-financed projects and reported high levels of delay (p. 14). The highest average delays occurred in the equipment/development type of project (54%), followed by non-standard buildings (39%), standard civil engineering (34%), non-standard civil engineering (15%) and standard building type of project (4%). In addition, the traditionally-procured projects had a high level of cost overruns. The highest occurred in the equipment/development type of project (214%), followed by non-standard civil engineering (66%), non-standard buildings (51%), standard civil engineering (44%) and standard building type of projects (24%).

Achieving value for money has also been identified by the Canadian Governement as the primary rationale for delivering infrastructure through PPP. The Canadian practitioners of PPPs defined value for money as a measure of the extent to which cost savings are achieved when delivering a public infrastructure project through a PPP relative to a traditional government-led procurement approach. Siemiatycki (2013) reported that PPP in Canada had been attractive because of delivering the project earlier than the agreed schedule:

> *'Public-private partnerships promise better value, timeliness and accountability for public infrastructure projects. That's exactly what the City of Winnipeg experienced with our 3.5 kilometre Chief Peguis Trail Extension. The project, including an underpass, multi-use pathway and pedestrian overpass, was completed one year ahead of schedule thanks, in large part, to this innovative approach.'*

Indonesia Government has experienced a number of delays in infrastructure projects such as Jakarta Monorail, Sunda Strait Bridge; and unsuccessfull projects such as Dumai Water Suply which has spent government fund for IDR 239 billion. This problem is similar to the problems in countries which have developed PPP earlier. However, very few arguments provided in Indonesia PPP investor guide which highlight value for money issue. This may indicate that the government is so far only concern on inviting private partners but put less attention on value for money they need to achieve from the

TABLE 4: PROBLEMS WITH CONVENTIONAL PUBLIC PROCUREMENT

NO	NAME OF PROJECT	COST OVERRUN	TOTAL SLIPPAGE IN COMPLETION DATE
1	Trident Submarine Shiplift and Berth (Faslane, Scotland)	Initial cost estimate £100m, final cost £314m	2 ½ years
2	Jubilee Line Extension	Initial cost estimate £2.1b, final cost some £3.5b	almost 2 years
3	The New En-Route air traffic control centre	Total initial cost estimate £475m, latest estimate £655m	5 years
4	Guy's Hospital	Initial cost estimate £36m, final cost £160m	over 3 years

Source: Treasury (2000, p. 18)

PPP. In addition, the guidance provided by the government has lack attention on the importance of output specification, which is the heart of the PPP procurement.

2. UNOFFICIAL REASONS

Failing to be convinced by Government, a number of reasons for using the PPP have been articulated by public policy observers in the UK. Since these reasons were not officially stated, they are described as unofficial reasons. These are off-balance sheet and ideological reasons.

I. OFF-BALANCE SHEET FINANCING

A number of studies reported that the use of the PPP was driven by the opportunity to have the asset recorded off-balance sheet in the Government accounts (Broadbent and Laughlin, 2002; Heald, 1997; Heald and Georgiou, 2011; Hodges and Mellett, 1999, 2012; McQuaid and Scherrer 2010, p. 30; Terry, 1996). The importance of this accounting instrument is to enable the Government to develop public infrastructure without increasing the level of public borrowing. This is because the rules imposed by the European Union on member state budget deficits and debt have potentially limited public borrowing (McQuaid and Scherrer, 2010). Based on its risk transfer methodology, the use of the PPP can camouflage an investment as 'a series of smaller annual revenue expenditures over the life of the project' and consequently allow the acquisition of new infrastructure without apparent increases in public borrowing (McQuaid and Scherrer, 2010, p. 30).

Heald and Georgiou (2011) identified that, up to October 2007, there were 87% of 618 PPP projects in the UK which were off-balance sheet. The Scottish Government and the Department for Children, Schools and Families in England were the two top departments in the UK with the largest number (114 and 98 respectively) and with the highest proportion (99% and 100% respectively) of off-balance sheet PPP projects. These figures show that all projects in the school sector in England and almost all projects in Scotland did pass the off-balance sheet requirement of TTTN1 through significant risks being transferred to the private sector. This situation, according to Heald (2003), may imply lower VFM for the public sector, since the accounting treatment was the dominant consideration in project selection rather than obtaining VFM from public expenditure.

In Indonesia context, off-balance sheet is not a critical issue as in the United Kingdom. Based on data release by trading indicators, the ratio of debt to GDP for Indonesia is only 26.11%, far below the United Kingdom of 90.60%. In addition, Indonesia has no restriction to have greater debt as imposed on European Countries under through 60% Maastricht debt criterion

II. IDEOLOGY

Ideology is suggested as another important unofficial reason by academics and political commentators to explain why the UK Government insisted on the use of the PPP. Referring to Government policy since the end of the 1970s, Edwards and Shaoul (2003, p. 397) asserted that public policy in the UK has been dominated by the neo-liberal agenda of privatising state-owned trading enterprises such as public corporations and Government Agencies. Similarly, the PPP has been designed to have the delivery of public sector support services and, increasingly, their core services provided by the private sector based on long-term contractual arrangements. Consequently, the Government and its agencies would become 'the procurer and regulator of service rather than the provider' (Edwards and Shaoul, 2003; Hatcher, 2006). Thus, the PPP policy was widely perceived as another way

of privatising public service delivery that could not be fully privatised for financial or political reasons (Edwards and Shaoul, 2003; Monbiot, 2002; Connolly et al, 2008). This approach, according to Broadbent and Laughlin (2002), was not a technical matter, but more an ideology:

> *There were strong ideological elements in the conception of PPP. An element of this is a belief that there should be a greater private sector involvement in the services that have been provided, in the past, by the UK's public and government authorities (p. 630).*

Criticism on the neoliberal agenda by the then President Susilo Bambang Yudoyono did exist during his administration. However, there is no specific rejection to the inception of PPP programs initiated by the Government as what happened in the UK. This can be understood for the following reasons. First, all PPP projects offered in Indonesia are for hard economic infrastructures and none of them in the category of social infrastructure such as school in the UK PPP. It is clearly said in the PPP guidance that the scope for the PPP are airports, sea and river ports, roads and bridges, railways, water supply and irrigation system, drinking water, waste water, solid waste, ICT, electricity and oil and gas. Second, high demand from the public for better infrastructure where they will not concern whether procured by the public or the private sector. Three, the new PPP projects is still at early phase and no risk had been transferred yet to the public such as extra cost they have to pay for the services provided. In addition, no transparency from the government to the public about the cost that the public will have to pay. In addition, the government will be likely to provide subsidy if the cost is too high for the public.

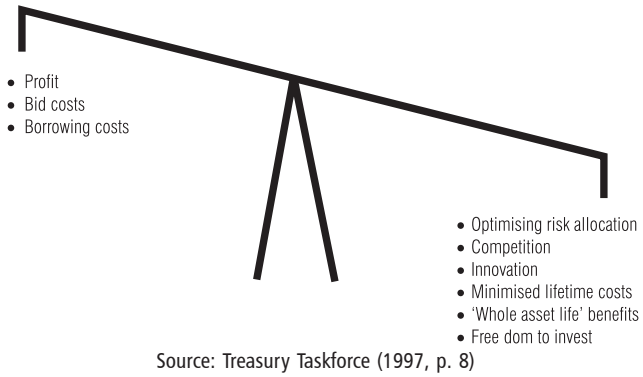
PPP VALUE FOR MONEY MECHANISM

The Treasury (2004a, p. 17) defined VFM as 'the optimum combination of whole life costs and quality'. It clarified that VFM is not about achieving the lowest initial price. In addition, the Treasury (2006b, p. 7) required VFM assessment to compare the potential or actual outcomes of the alternative procurement options. In its early guidance, the Treasury Taskforce (1999a) suggested the PPP procurement team make VFM judgements based on the whole life costs rather than individual cost components. The whole life costs should include the future upgrade/maintenance requirements of the asset and its residual value if the asset reverts to the public sector at the end of the contract:

> *As PPP is about the delivery of a stream of services over the longer term, judgements should be made on whole life costs rather than on individual cost components incurred at particular junctures. The evaluation of bids needs to focus on the overall cost of services over the life of the contract rather than on the phasing of items of expenditure or individual cost components within it. For example, in competing for the same service requirement, two rival bidders may have different approaches, with one choosing to have high upfront capital investment with lower future upgrade/ maintenance requirements, and the other relatively low initial capital investment but with more frequent renewals and upgrades. The procurer should concern itself with the overall NPV of bidders' unitary charges rather than the mix or balance of individual components within it. If the asset reverts to the public sector at the end of the contract, the procurer should also assess the residual value of that asset to get a whole life value of each bidder's proposals (Treasury Taskforce, 1999a, para. 4.2.1)*

The Treasury Taskforce (1997, p. 8) acknowledged that there are extra costs incurred from the use of the PPP. These are provider's profit, bid costs and borrowing costs. However, it was claimed that the extra costs incurred can be outweighed by the benefits derived from the PPP, as shown in Figure 3.

FIGURE 3: THE VFM BALANCE

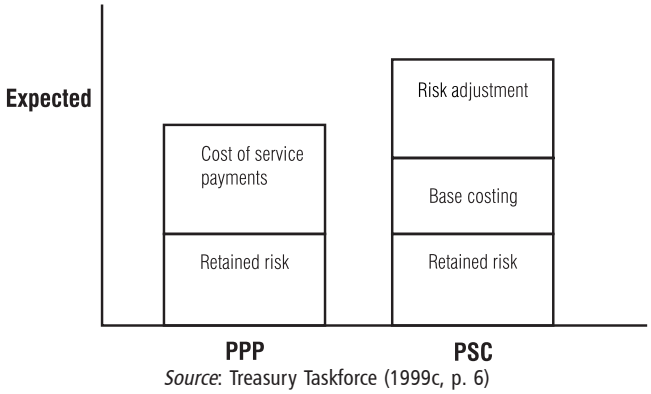


Source: Treasury Taskforce (1997, p. 8)

To measure value for money of a PPP project, most countries used Public Sector Comparator as assessment tool (Grimsey and Lewis, 2004). UK Policy Statement

Number 2 (Treasury Taskforce, 1998b, para. 1.3.2) defines the PSC as 'a cost estimate based on the assumption that assets are acquired through conventional funding and that the procurer retains significant managerial responsibility and exposure to risk'. Grimsey and Lewis (2004, p. 137) considered the PSC as a benchmark cost of providing required services under conventional procurement. The PSC is to be produced prior to the procurement of a project, to test the potential VFM of procurement options (Treasury, 2003a, p. 7). The overview of the cost structure of the PSC and the PPP is shown in Figure 4. Both the PSC and PPP include the same retained risk, which is the risk retained by the public sector. In addition to the retained risk, the PSC should include risk adjustment and project base costs. On the other hand, the PPP cost structure only includes the cost of service payments in addition to the retained risks.

FIGURE 4: VALUE FOR MONEY COMPARISON BETWEEN A PSC AND A PPPBID



Source: Treasury Taskforce (1999c, p. 6)

Under the PSC, all relevant and material risks should be identified and assigned (Treasury Taskforce, 1999c, p. 40). Some risks could be clearly classified as transferable to the supplier, such as design risks, or as retained in the public sector, such as policy risks. However, there are risks which are potentially either transferable or retainable. These are classified as negotiable risks and could be partially transferred to the private sector according to a given formula (p. 40). The procuring authority is suggested to include in the PSC the estimates of the basic costs of capital assets, including any fit-out costs needed to convert an existing property to the required use (Treasury Taskforce, 1999c, p. 14). Besides the upfront construction costs, the basic capital costs should also include the full lifecycle costs of maintaining the assets in order to deliver the output specification (examples of these costs are the replacement of lifts, rewiring or changes in equipments with shorter life expectancies). The basic capital cost estimation in the PSC should reflect all resource costs of the project, including the opportunity cost of the asset if sold or used for another purpose. All the assumptions should follow the latest experience of conventional procurement, such as assumptions about construction techniques. Besides basic capital costs, basic operating costs should also be included in the Public Sector Comparitor. The operating costs include the costs of services according to the output specification over the period of contract (Treasury Taskforce, 1999c, p. 16).

Indonesia PPP guidance acknowledges common PPP practices to use PSC as tool for value for money assessment. However, the guidance declines to use the PSC for reasons of being unrealistic to be applied in Indonesia due to limited government budget and capacity.

> *Traditional VfM analysis determines whether a PPP approach will deliver the service or infrastructure more effectively and at less cost than through standard public sector means, as represented by the Public Sector Comparator (PSC). However, this traditional approach is based on assumptions that do not reflect conditions in Indonesia. For example, a traditional VfM analysis using a PSC implicitly assumes that public sector development of the infrastructure is a realistic option. Due to limited government budgets and capacity, it may not be an option in Indonesia. (CMEA, 2011)*

As alternative, Indonesian PPP uses project modalities approach with a sequence steps. First, a full range of project modalities from fully public to fully private are identified. Second, Parametersthat can affect project success are identified, which include social, institutional, technical and economic factors. Third, modalities are evaluated qualitatively relative to one another against these parameters to determine the most promising modalities. Fourth, available risk mitigation mechanisms are then considered, which may re-order or expand the feasible modalities. Finally, the top-ranked modalities are then evaluated quantitatively using a financial model to determine which modality yields the highest revenue constrained project net present value. The revenue

constraint is applied to reflect end-user willingness to pay or off-taker avoided cost. Problems with this methodology is lack attention on identifying risk and transferring them to the best party able to manage it as compared to the PSC model. Under the PSC, from the very beginning risk should be identified and that process is helpful in making clear private partner responsibility. In addition, a thorough process is essential in the implementing risk transfer mechanism.

Under common PPP approach some factors are identified to result in better value for money (Treasury Taskforce, 1997, para. 3.08). These are: (1) bundling of design, build and service operation; (2) output specification that encourages innovative design, re-engineering, avoidance of over-specification, new materials or more efficient maintenance (including guaranteed maintenance at the appropriate time); and (3) efficient allocation of risks to the parties best able to manage them at least cost. Details on how the above aspects contribute to VFM are now discussed and compared with Indonesia experience.

1. PPP BUNDLING

Martimort and Pouyet (2008) explained some circumstances where PPP methodology would perform better than conventional procurement. They proposed that, in a situation where a performance contract can be written and infrastructure design can save operating costs, bundling the tasks of building and managing the assets would be the optimal organisational structure. The argument is that private consortia can better internalise the impact of the improved infrastructure quality on operating costs. Consequently, a private consortium will strive to produce better design of the infrastructure in order to gain a bonus by lower operating costs. These benefits do not exist under conventional procurement, as the building and managing asset tasks are undertaken by separate entities. De Bettignies and Ross (2010) added that better performance under bundling is caused by the efforts made by the PPP builder and operator. As the builder's efforts can have a positive impact in reducing operating cost, they would exert the first-best level of effort to increase project quality. By contrast, under unbundling, the builder would only exert 'a strictly positive but second-level effort'. In addition, Iossa and Martimort (2008, p. 16) suggested that the effort level with bundling is higher.

PPP projects in Indonesia do not necessary follow the pure method of project bundling in overseas. This can be seen from the establishment of PT. Indonesia Infrastructure Financing (PT. IIF) by Indonesian Government through its state owned enterprise PT. Sarana Multi Infrastructure (PT SMI) to provide funding towards commercially feasible projects. To increase its capacity PT IIF received loan from World Bank and Asian Development Bank. This company plays it role in increasing the availability of equity and long term debt, particularly rupiah available for private infrastructure investment in Indonesia. Therefore, the project company in Indonesia may consist of project sponsors, either from the private sector including local and foreign invetsors, and/or government through state-owned enterprise. This mechanism follow the Canadian PPP where some projects may have upfront finance by the Government and only one third as private finance (Siemiatycki, 2013). The advantage of this approach is to reduce high cost of private finance which is usually more expensive than public funds.

2. PPP OUTPUT SPECIFICATION AND VALUE FOR MONEY

The Treasury Taskforce (1999c, p. 10) defines output specification as 'a statement of needs to be satisfied by the procurement of external resources'. It is an instrument to specify what the public sector client wants to procure and what the supplier is expected to provide. This instrument is used by the public sector to construct the PSC, and is utilised by the private sector to prepare PPP bids.

The Treasury (2003b, p. 33) stated that the output specification is different from the input specification approach under conventional procurement. Under conventional procurement, the procuring authority describes precisely the work required to deliver particular services. This is then tendered for to secure competitive pricing and the most economically advantageous proposal for the construction. However, 4Ps (2001), a consulting body for PPP projects established by the Local Government Association and Partnerships UK, stated that, if the design and plan produced by the public sector was inappropriate, it is the public sector that will bear the cost to put the construction back on track if costs increase because of project delays. Consequently, conventional procurement has the potential to cost more than the original estimated cost, or can fail to meet the initial

output objectives. In addition, a number of uncertainties in terms of building lifecycle maintenance, ongoing provision of services, and efficiency of facilities, would exist after asset construction (4Ps, 2001).

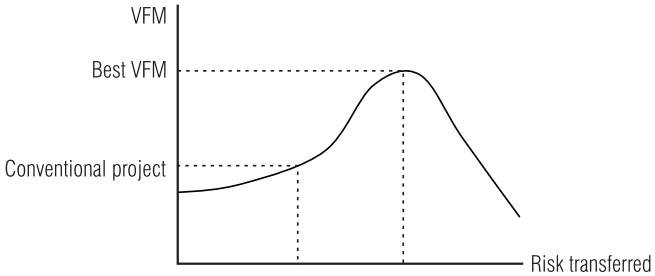
Under PPP procurement, the procuring authority only specifies the services required (Treasury, 2003a). The selection of a preferred bidder is based on the competition to offer better whole life costs and the quality to meet users' requirement and not necessarily based on the one with lower construction cost. According to 4Ps (2001), this approach would encourage a focus on strategic needs rather than on 'the history and detail of current provision' (p. 5). A proper output specification would drive the private sector to come up with new ideas about the design, construction and operation of schools (p. 6). As this approach also encourages bidders to develop means to deliver the outputs within a fixed performance-related pricing mechanism, 4Ps (2001, p. 6) stated that the PPP should 'lead to better designed and operated schools in the longer term'. The Treasury (2003a) also argued that the use of an output specification would benefit the public sector as this can drive the private sector to meet the desired output objectives by using their best expertise and know how to deliver the service.

Although output specification is at the heart of the use of the PPP, guideline on PPP performance standards in Indonesia is very limited. In the investor guideline issued by the Coordinating Ministry of Economic Affairs, performance standards is one of the elements to be included in the document of Cooperation Agreement. However, there is no further details about how the performance standards will be used and what mechanism will be applied to record the performance. Transparency and the existing of clear guidance in this area is very much needed as much of the government needs private involvement. Value for money study in the country with mature PPP phase shows the important of clarity in output specification. Yaya's (2013) study shows that projects with poor output specification is less value for money than those with thorough output specification.

3. PPP RISK TRANSFER AND VALUE FOR MONEY

Risk transfer is defined by the Treasury Taskforce (1999c, p. 63) as 'the process of moving the responsibility for the financial consequences of a risk from the public to the private sector'. This concept is based on the public sector's efforts to find a solution for cost overruns in public infrastructure procurement. The TTTN Number 5 (Treasury Taskforce, 1999c, p. 8) stated that an optimum risk transfer can lead to 'dramatic improvements in value for money'. However, OECD (2008, p. 49) suggested that risk allocation to the party best able to manage it does not mean maximum risk transfer. Figure 5 shows that risk transfer could improve VFM to a certain level after which VFM declines as the result of more risk transfer.

FIGURE 5: RISK TRANSFER AND OPTIMAL VFM



Source: Treasury Taskforce (1997, p. 11)

Theoretically, VFM is improved by transferring risk to the private sector which can reduce it in terms of the probability of occurrence or financial consequences, if the risks do materialise. However, VFM will decline if the public sector keeps transferring risks which cannot be best managed by the private sector. The decline is caused by the benefits of risk transfer being outweighed by the premium charged by the private sector. Furthermore, having too much risk transfer may result in the public sector paying a premium for something that will not be delivered. This is because there are many PPP projects with services which cannot be neglected, such as health and education. Consequently, when problems arise, the public sector would have to step in, thus providing an implicit guarantee to the private sector. It is the optimum rather than the maximum total risk transfer which should be aimed at by the PPP procurement method.

Under Indonesian PPP framework, risk transfer issues seem not properly addressed. This can be inferred from no clear guidance about what penalty will be imposed for not meeting the standards and and how it will be executed.

CONCLUSION

The development of PPP around the world has

attracted Indonesia Government to use this approach intensively for its new infrastructure projects. Ambitious target has been set up by the Government to raise IDR 980 trillion under PPP to fund its IDR 1,430 trillion new infrastructure projects over the period 2010-2014. Reasons for using the PPP follow the argument of other countries of the need for greater investment and better value for money. However, the PPP framework in Indonesia does not address properly the issue of output specification and risk transfer which is the key point to achieve better value for money.

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